



Introductory Section

In comparison to the more than \$2 billion in benefits disbursed by the Retirement Systems, personal income derived in the Palmetto State from hospitals equaled \$1.766 billion.*

Hospitals include those institutions that provide medical, diagnostic, and treatment services that include physician, nursing, and other health services to inpatients and the specialized accommodation services required by inpatients. Hospitals provide inpatient health services, many of which can only be provided using the specialized facilities and equipment that form a significant and integral part of the production process. Hospitals may also provide outpatient services as a secondary activity.

*Based on Bureau of Economic Analysis data for 2007.

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Mark Sanford, Chairman
Governor
Converse A. Chellis, III, CPA
State Treasurer
Richard Eckstrom
Comptroller General

State Budget and Control Board
South Carolina Retirement Systems
Retiring South Carolina's Public Workforce
For Life

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Peggy G. Boykin, CPA
Director

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Hugh K. Leatherman, Sr.
Chairman,
Senate Finance Committee
Daniel T. Cooper
Chairman,
Ways and Means Committee
Frank W. Fusco
Executive Director

LETTER OF TRANSMITTAL

November 26, 2008

The Honorable Mark Sanford, Governor
and
State Budget and Control Board
State of South Carolina

Gentlemen:

We are pleased to present the *Comprehensive Annual Financial Report* (CAFR) of the South Carolina Retirement Systems for the fiscal year ended June 30, 2008. The South Carolina Retirement Systems is required by Section 9-1-300 of the South Carolina Code of Laws to publish annually a report of the fiscal transactions of the system and this CAFR fulfills that statutory requirement. Since the Retirement Systems is a part of the primary government of the state of South Carolina, the Systems' financial information is also included in the comprehensive annual financial report of the state. Responsibility for both the accuracy of the data, and the completeness and reliability of the presentation, including all disclosures, rests with the management of the Systems. To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and results of the Systems.

The CAFR was prepared to conform to the principles of governmental accounting and reporting set forth by the Governmental Accounting Standards Board (GASB). Transactions of the Systems are reported on the accrual basis of accounting. Sufficient internal accounting controls exist to provide reasonable assurance regarding the safekeeping of assets and fair presentation of the financial statements and supporting schedules. The financial statements presented in this CAFR have been independently audited by Rogers Laban, PA, Certified Public Accountants, under the direction of the State Auditor's Office. Rogers Laban issued an unqualified opinion, which means that based upon the audit, they concluded that the financial statements were fairly presented in all material aspects and free from material misstatement. In accordance with Governmental Auditing Standards, as part of obtaining reasonable assurance about whether the Systems' financial statements are free of material misstatement, Rogers Laban also considered internal controls over financial reporting and compliance with certain provision of laws, regulations, contracts, and other matters. Although independent auditors cannot guarantee the accuracy of the statements, they do have a reasonable basis for the opinion they render. The independent auditor's report is presented as the first component of the financial section of this report.

Profile of the Systems

The South Carolina Retirement Systems administers five defined benefit pension plans that provide lifetime retirement annuities, disability benefits and death benefits to eligible members. The plans' terms specify the amount of pension benefits to be provided at a future date or after a certain period of time. The amount specified is a function of a formula based on years of service, compensation, and age. Our administrative and reporting structure is outlined in the introductory section of this report.

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This report contains information on the following defined benefit pension trust funds:

- The South Carolina Retirement System (**SCRS**) was established July 1, 1945, to provide retirement and other benefits for teachers and employees of the state and its political subdivisions.
- The Police Officers Retirement System (**PORS**) was established July 1, 1962, to provide retirement and other benefits to police officers and firefighters.
- The Retirement System for Members of the General Assembly of the State of South Carolina (**GARS**) was established January 1, 1966, to provide retirement and other benefits to members of the General Assembly.
- The Retirement System for Judges and Solicitors of the State of South Carolina (**JSRS**) was established July 1, 1979, to provide retirement and other benefits to state Judges and Solicitors.
- The National Guard Retirement System (**NGRS**) was established July 1, 1975, to provide supplemental retirement benefits to members who served in the South Carolina National Guard.

Fiscal Year 2008 Highlights

During fiscal year 2008, South Carolina experienced significant progress towards protecting the purchasing power of our state's retired public workforce and securing the financial stability of the state's public pension plans. The South Carolina General Assembly enacted legislation that stabilized funding of the Retirement Systems and placed restrictions on future cost-of-living adjustment (COLA) increases that would otherwise further erode the plan assets. This represents a giant step forward in limiting ad hoc COLAs that have historically placed a significant drain on the system. Over the years, ad hoc COLAs have steadily increased the unfunded actuarial accrued liability which inhibited progress in improving the funding of the plan.

The South Carolina Retirement System Investment Commission's (RSIC) redeployment and reallocation of the Retirement Systems' assets has been substantially implemented as a result of an amendment to the state constitution, which effectively broadened the opportunity set for diversifying the investments in the portfolio. The attainment of the target allocation will extend into fiscal year 2009.

From an operational perspective of administering the plans, the South Carolina Retirement Systems continued to maintain high stakeholder satisfaction, while maximizing resources to balance a very demanding workload. A new Communication and Education Unit was established to meet the broad strategic goal of educating all of the Systems' stakeholders. We repositioned the Electronic Employer Services (EES) from Customer Services to Financial Employer Services in an effort to more appropriately align employer reporting functions and improve customer service to our covered employers. Preliminary efforts were also initiated to implement a compliance function to review various financial transactions reported from covered employers for compliance with regulations and procedures.

South Carolina General Assembly Passes COLA Legislation

The South Carolina General Assembly passed House Bill 4876 which provides an automatic annual COLA of up to 2 percent each July for eligible annuity recipients of the South Carolina Retirement System (SCRS) and the Police Officers Retirement System (PORS).

Passage of this bill, which included recommendations from the State Treasurer's COLA Task Force, is important because future ad hoc COLAs, those that are neither guaranteed nor pre-funded, are not included in a retirement plan's actuarial liabilities until the time at which they are approved. Once ad hoc COLAs are approved, they must be paid using assets of the retirement trust funds or through some other funding mechanism. Historically, ad hoc COLAs granted to our retirees have been paid primarily from the assets of the retirement trust funds.

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By guaranteeing an annual COLA and providing a stabilized funding mechanism, the cost of the COLA is recognized as a liability for actuarial purposes up front. Additionally, by guaranteeing and pre-funding a COLA, eligible retirees can count on protection of their future purchasing power. The automatic COLA provisions became effective June 17, 2008, the date the State Budget and Control Board, as trustees for the Retirement Systems, approved an increase in the Retirement Systems' assumed rate of investment return to 8 percent from 7.25 percent.

House Bill 4876 also set limits on COLAs. If the Consumer Price Index (CPI) as of the previous December 31 is less than 2 percent, the automatic COLA would equal the increase in the CPI. If the CPI is greater than 2 percent, the Board has authorization to increase the COLA beyond the automatic annual 2 percent up to the total percentage increase in CPI or 4 percent, whichever is less. However, the increase beyond the automatic 2 percent may only be granted when certain conditions are met. Previously, ad hoc COLAs could be granted as long as the system(s) could support the funding of the COLA and maintain an unfunded liability amortization period of 30 years or less.

This legislation protects the systems from increased actuarial liabilities due to ad hoc COLAs by preventing ad hoc COLAs from being granted if a system's amortization period for the prior year's unfunded liability exceeds 25 years and by prohibiting employer contribution rate increases to support the grant of an ad hoc COLA. The provisions also require that the system's amortization period must have decreased by one year in the most recently concluded fiscal year valuation and that the estimated funded ratio must not decrease.

Internal Revenue Code Compliance

The South Carolina Retirement Systems periodically conducts a review of retirement statutes to ensure continued compliance with the Internal Revenue Code (IRC). Likewise, the Internal Revenue Service (IRS) periodically reviews the Retirement Systems' "plan documents" to ensure compliance with the IRC. The statutes governing the Retirement Systems are considered the plan documents for IRS/IRC purposes.

In addition to the COLA provisions referenced above, House Bill 4876 also included provisions that modified retirement statutes to ensure the Retirement Systems' continued compliance with the IRC. Most of the provisions were technical in nature. One provision affected a member's ability to choose a payment plan that provides for a continuing survivor annuity benefit. While the IRC allows a spouse and multiple beneficiaries, regardless of age, to receive a 100 percent survivor benefit, a sole beneficiary who is not the member's spouse must be within certain age difference limits as determined by an IRC formula that is based on the retiring member's age, the beneficiary's age, and the difference between the member's age in the year of retirement and age 70. Another provision of the legislation required that the Retirement Systems comply with IRC-required distribution guidelines.

Transition of Custodial Bank

The Bank of New York (BNY) has been the custodial bank for investments of the South Carolina Retirement Systems for many years. With the bank merger between BNY and Mellon Bank, the Retirement Systems' Investment Accounting Unit and RSIC staff worked closely with BNY Mellon to migrate to Mellon's superior operating "Workbench" platform effective May 1, 2008. A team comprised of individuals from each organization successfully completed the transition project, which included developing and implementing automated general ledger interfaces for the various investment asset classes.

Ranking Among Peer Pension Plans

The South Carolina Retirement Systems participates biennially in a public pension plan benchmarking analysis conducted by Cost Effectiveness Management, Inc., (CEM). Seventy-four public pension plans participated in the CEM survey for 2007, which marked the seventh year of participation for the Retirement Systems.

Although the Retirement Systems is a customer centric organization, we are also a division of South Carolina state government and as such, must adhere to stringent budgetary guidelines. According to the CEM report, the South Carolina Retirement Systems' total adjusted administrative cost per member was \$47 in comparison to a peer median cost of \$77. Our low administrative cost is achieved through the efficient and proactive deployment of automated systems and appropriately allocated human resources.

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To continue to provide best practices service levels to our stakeholders, the Retirement Systems must expend the resources necessary to both maintain our infrastructure and expand our technological and human resources. Our infrastructure has been stagnated by mandatory changes required by legislation and court rulings. We have also utilized our human resources far beyond capacity.

Investment Returns

Given the volatility and uncertainty of the investment market, there is widespread concern and anxiety; however, retirement benefits provided by the defined benefit plans administered by the South Carolina Retirement Systems are protected and secure. Defined benefit plans have vastly long-term investment time horizons; so, while the financial markets are currently experiencing significant volatility, the assets of the Retirement Systems are invested in a broadly diversified manner to help mitigate risks. Member benefits under the Retirement Systems' defined benefit plans are protected because they are defined by state statute and are not dependent on individual account balances or investment returns.

Although the Retirement Systems posted a negative return for the fiscal year, our investments outperformed our benchmarks. Wilshire Associates, a leading global investment technology, investment consulting, and investment management firm maintains a Trust Universe Comparison Service (TUCS) that is considered the most widely accepted benchmark for the performance of institutional assets. According to the TUCS database maintained for the period ended June 30, 2008, the average investment return of our peers was negative 4.36 percent, in comparison to our negative 2.56 percent for the same time period.

Summary of Financial Condition

The funding objective of the pension trust funds is to meet future benefit obligations of retirees and beneficiaries through contributions and investment earnings. Each year, our external consulting actuaries determine the actuarial soundness of the plans based on long term obligations and the sufficiency of current contribution levels to fund the liabilities of each plan over a reasonable time frame. In our most recent valuations dated July 1, 2007, our actuarial consultants concluded that all systems are operating on an actuarially sound basis. All five systems are considered to be adequately funded within the Governmental Accounting Board's standards and the Budget and Control Board's policy that requires actuarial liabilities be funded within 30 years. The funded ratio for SCRS, which represents the largest membership of the five plans, improved slightly from 69.6 percent to 69.7 percent. Accordingly, the period for amortizing SCRS' unfunded actuarial accrued liability declined slightly from 30 years to 29 years. A 2.4 percent COLA was granted effective July 1, 2007, 1.4 percent of which was in the form of an ad hoc COLA that increased the unfunded liability and amortization period; however, a 0.18 percent increase in the employer contribution rate effective July 1, 2008, offset the increase such that there was no net effect of the ad hoc COLA. In accordance with the actuarial smoothing technique, the plan also recognized an actuarial gain in the July 1, 2007, valuation as a result of recognizing a portion of the fiscal year 2007 investment returns. Other factors that are normal in the course of plan experience, such as non-investment related experience activity, offset actuarial gains that were attained from recognizing the smoothing of investment returns.

The current funded ratios of the five plans range from a low of 28.8 percent for NGRS to a high of 84.7 percent for PORS. The NGRS has a very low funded ratio because historically the plan was not funded on an actuarial sound basis. In 2006, the General Assembly made a commitment to ensure the plan would be sufficiently funded prospectively and transferred administrative responsibility from the Adjutant General's Office to the South Carolina Retirement Systems. Now recurring funds are set aside in the state's annual budget each year to fund NGRS over an amortization period that does not exceed 30 years and we anticipate improvement in the funded ratio. More detailed information regarding the financial condition of the pension trust funds can be found in the financial and actuarial sections of this report.

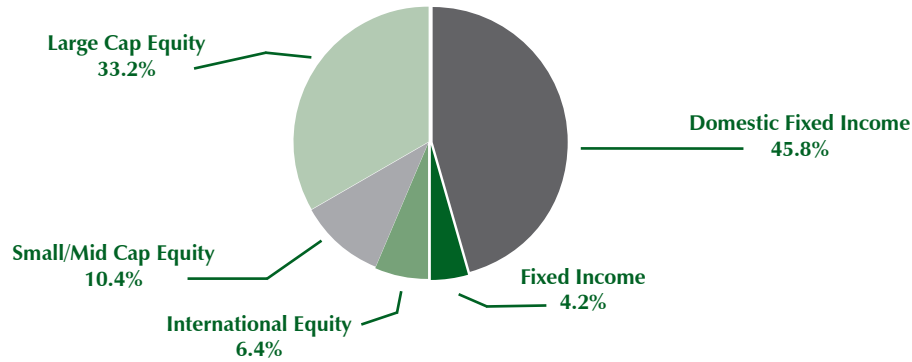
An optimally diversified investment portfolio is designed to generate long-term returns sufficient to ensure that the program is financially sound. While the Systems' investment performance was previously limited by our state constitution and state statute, the RSIC worked diligently to continue implementation of a modern-day asset allocation policy. With the help of the RSIC's investment consultants, New England Pension Consultants, the RSIC deployed investments across a progressive asset allocation designed to reduce the amount of risk while aiming to

Introductory Section

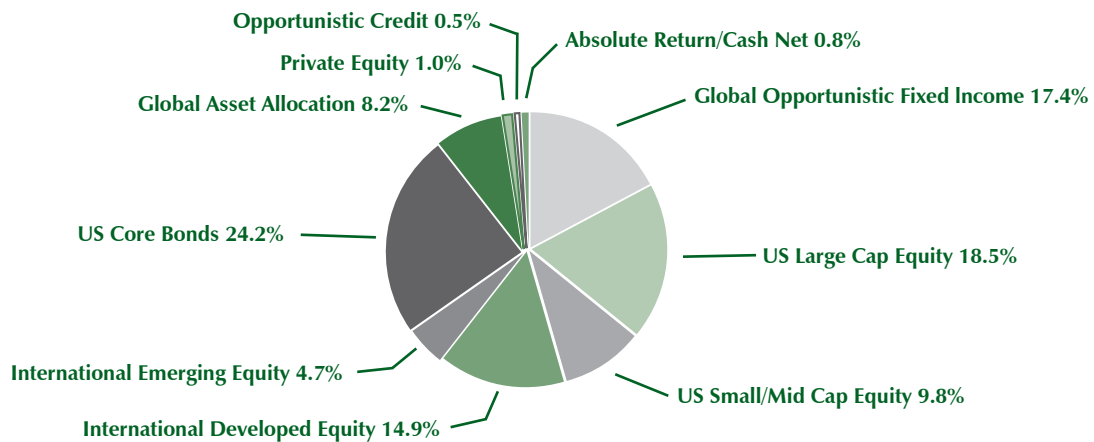
increase overall returns. In addition to the RSIC's efforts to gain immediate exposure to almost all of the new asset classes, planned strategies to fully implement the target allocation which includes more private equity agreements, real estate, and other entrepreneurial opportunities in the hedge fund arena will take several years to complete.

The following charts summarize the Investment Commission's progress toward diversifying the Retirement Systems' portfolio from the prior fiscal year and the long-term target allocation.

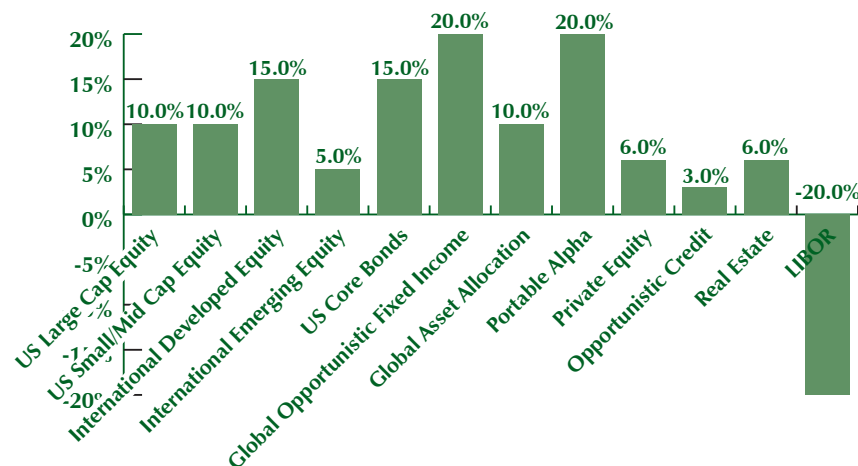
Actual Asset Allocation as of June 30, 2007



Actual Asset Allocation as of June 30, 2008



Target Asset Allocation



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For the year ended June 30, 2008, the combined Systems' investment portfolio produced a total aggregate investment return of negative 2.56 percent. Current year performance was significantly less than the actuarial assumed rate of return utilized for actuary valuation purposes; however, the actuarial smoothing methodology offsets any investment gains and shortfalls over a period of years to mitigate market volatility. The State Budget and Control Board, as trustees for the Retirement Systems, approved actuarial assumption changes that will be effective with the next actuarial valuation dated July 1, 2008. Approved changes include increasing the Retirement Systems' assumed rate of investment return to 8 percent from 7.25 percent and extending the smoothing period from five years to 10 years.

Investment performance in comparison to the assumed rate of return is a significant factor in our actuarial valuations. As referred to above, our actuarial consultants use an actuarial asset valuation method that recognizes a portion of the difference between the actual market value of assets and the expected actuarial value of assets, based on the assumed investment rate of return of 8 percent. This method recognizes 20 percent of the difference between market and expected actuarial value each year and guarantees that any gain or loss is recognized over a 10-year period. The actuarial value of assets is limited to a range between 80 percent and 120 percent of market value. This actuarial asset valuation method dampens year-to-year fluctuations, smoothes the effect of volatility in the market and helps provide a consistent estimate of the value of assets. Detailed investment results for fiscal year 2008 can be found within both the financial and investment sections of this report.

It is paramount to note that the five defined benefit plans administered by the South Carolina Retirement Systems are considered actuarially sound. Both annuity benefits and a guaranteed 2 percent COLA under SCRS and PORS are sufficiently funded based on current contribution levels. For additional financial information, please refer to management's discussion and analysis, as well as the financial statements, and the schedules included in the financial section of this report.

Certificate of Achievement

The Government Finance Officers Association (GFOA) of the United States and Canada awarded a Certificate of Achievement for Excellence in Financial Reporting to the South Carolina Retirement Systems for its CAFR for the fiscal year ended June 30, 2007. The Certificate of Achievement is a prestigious national award recognizing excellence in the preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report, the contents of which meet or exceed program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid only for a period of one year. The Systems has received a Certificate of Achievement for each of the last 21 consecutive years (fiscal years ended 1987-2007). We believe this 22nd issue of our annual report continues to conform to the Certificate of Achievement Program requirements, and we are submitting it to the GFOA for consideration again this year.

Public Pension Standards Award

The South Carolina Retirement Systems also received the Public Pension Coordinating Council's Public Pension Standards 2008 Award. This is the fifth consecutive year during which the Retirement Systems applied for and received the Council's award in recognition of meeting professional plan design and administration standards. The Public Pension Coordinating Council is a confederation of the National Association of State Retirement Administrators, the National Conference on Public Employee Retirement Systems, and the National Council on Teacher Retirement.


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Acknowledgments

The compilation of this report reflects the combined efforts of the staff of the South Carolina Retirement Systems functioning under your leadership. The report is intended to provide comprehensive and reliable information about the Systems, to demonstrate compliance with legal provisions, and to allow for the evaluation of responsible stewardship of the funds of the Systems.

We express our gratitude to the members of the Board, the staff, the consultants, and the many people who have worked so diligently to assure the continued successful operation of the Systems.

Respectfully submitted,


Peggy G. Boykin, CPA
Director


Tammy B. Davis, CPA
Assistant Director, Payroll, Financial and Actuarial Reporting





Introductory Section

Governing Board and Administration

Governing Board - SC State Budget and Control Board

Mark Sanford, Chairman	Governor
Converse A. Chellis, III, CPA	State Treasurer
Richard Eckstrom	Comptroller General
Hugh K. Leatherman, Sr.	Chairman, Senate Finance Committee
Daniel T. Cooper	Chairman, House Ways and Means Committee
Frank W. Fusco	Executive Director

Retirement System Investment Commission¹

Reynolds Williams	Chairman
Converse A. Chellis, III, CPA	State Treasurer
Blaine Ewing, III	
James R. Powers	Vice Chairman
Allen R. Gillespie, CFA	
Robert L. Borden, CFA	Chief Investment Officer
Nancy E. Shealy	Administrative Director and General Counsel

Investment Consultant

New England Pension Consultants

Consulting Actuaries

Milliman Consultants and Actuaries
Cavanaugh Macdonald Consulting, LLC

Retirement Systems Executive Management

Peggy G. Boykin, CPA	Director
Sarah N. Corbett, CPA	Assistant Director – Administration
Tammy B. Davis, CPA	Assistant Director – Payroll, Financial and Actuarial Reporting
Amanda J. Green	Assistant Director – Customer Claims
Lisa Phipps	Assistant Director – Information Technology
Travis Turner, CPA	Assistant Director – Financial Employer Services
Jamella Williams	Assistant Director – Customer Services
David Avant	General Counsel – Retirement Systems
Gwen Bynoe	Legislative Liaison
Jocelyn Caldwell	Project Management Officer
Megan B. Lightle	Manager, Communication and Education
John Page	Internal Auditor

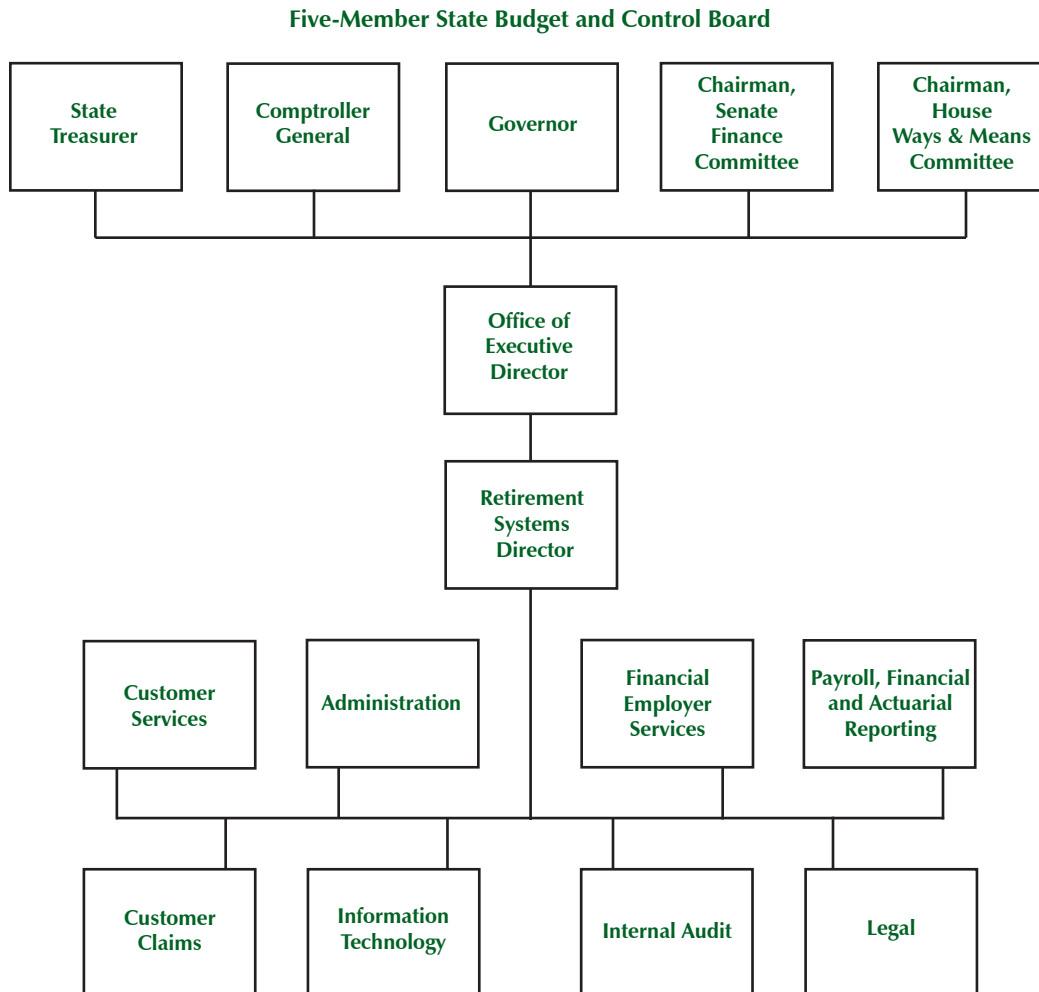
Retirement Systems Staff Responsible for Compilation of CAFR

Tammy B. Davis, CPA	Payroll, Financial and Actuarial Reporting
Ashley McAdoo, CPA	Payroll, Financial and Actuarial Reporting
Faith Wright	Payroll, Financial and Actuarial Reporting
Megan B. Lightle	Manager, Communication and Education
Angie Warren	Public Information Coordinator

¹Refer to pages 77-79 for a complete list of investment managers.

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Organizational Chart



Introductory Section

Organizational Description

The structural organization of the Systems is depicted in the organizational chart on page 17. A brief description of the primary functions performed by each department follows:

Administration

Responsible for managerial, budgetary, and administrative oversight of all division operations; physical plant issues, operations, and maintenance; procurement; human resources activities; communications and public information; accounts payable; postal center operations; and courier services. Also responsible for training employers in all aspects of the Retirement Systems' member benefits, reporting procedures, and the Internet-accessed employer information system; meeting with employees as requested to present benefit overviews and pre-retirement education programs; and coordinating and conducting retirement seminars designed to better prepare members whose retirement is imminent.

Payroll, Financial and Actuarial Reporting

Functioning as chief financial office for the Retirement Systems, responsibilities encompass maintaining comprehensive financial accounting systems, including actuary, investments and disbursements of benefit payments, for the five statutorily defined benefit retirement plans. This department is responsible for preparation of the *Comprehensive Annual Financial Report* and *Popular Annual Financial Report* as well as staffing accounting roles for disbursing funds and reporting of financial data; tax reporting; managing daily financial operations; establishing financial policies and procedures; and communication related to actuarial valuations, legal issues and fiscal impact of proposed legislative changes. Benefit payments are disbursed in the form of monthly annuities, TERI distributions, refunds to terminated members, and death payments to beneficiaries.

Customer Claims

Responsible for the processing of customer claims relating to annuities, refunds, or death claims; the computation of the cost for purchases of prior service for all members of the Retirement Systems; and the auditing of service credit for our membership.

Information Technology

Responsible for the design, implementation and control of all automated applications within the Systems; and the maintenance of complete historical records of each member via digital imaging.

Financial Employer Services

Responsible for determining the average final compensation to be used in calculating a member's annuity benefit at retirement; collecting and allocating member and employer contributions; maintaining membership enrollment and beneficiary information; and the State Optional Retirement Program.

Customer Services

Responsible for member consultations (in person, by telephone, or on-line via the Internet) in all phases of retirement operations.

Legal

Responsible for representing the South Carolina Retirement Systems in matters before circuit and appellate courts and administrative bodies, and for providing program support to the management of the South Carolina Retirement Systems.

Internal Audit

Responsible for providing an independent appraisal function to examine and evaluate processes and policies, and for providing assurance to management regarding the internal control structure of the division.